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Taxation in Panama

Deloitte, Haskins & Sells

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International Tax and Business Service

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This book is based on the latest information available to Deloitte Haskins & Sells as of the above date. The office of Deloitte Haskins & Sells in Panama is located at the following address:

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Taxation in Panama is part of a series that presents information on taxation in various countries of the world. The book is intended to supply information of a general character regarding taxation in Panama for use as background when considering the conduct of business in that country. Specific questions should be answered by reference to the laws and regulations of the country and by consultation with professional advisors in the light of the particular circumstances.

Taxation in Panama is published in two forms: in a loose-leaf edition and as a bound book. Only the loose-leaf edition may be supplemented or revised. These supplements will appear on blue-colored sheets inserted at the end of the book. These supplementary pages will be keyed to the original text by chapter and section numbers and should always be read in connection with the original text. In addition, revised information may be presented on pages inserted in the basic text to replace original pages. Revisions of this type are indicated by a date that appears on the bottom of each replacement page.

Rules governing taxation are subject to change and reinterpretation, in many cases with little or no advance notice. The information in this book is based on material available to Deloitte Haskins & Sells as of November 1978.

Taxation in Panama

Part 4 Rate Tables and Appendices

Part 1:
The Tax System

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Tax Legislation and Administration

1.01 Enactment of Tax Legislation

Panama's government is divided by the constitution into legislative, executive, and judicial branches. The legislative branch consists of the National Assembly whose membership is determined by popular election.

The power to tax rests with the national government through legislation enacted by the National Assembly and with municipalities. Income is taxed only by the national government. Other national taxes are outlined in Chapters 14, 15, and 16. Generally, national tax legislation is introduced by the executive branch and discussed, amended, approved, or abrogated by the National Assembly. The President's signature is necessary before a bill can become law.

In addition to the legislative taxing power, the National Assembly has the power to delegate authority to the President to enforce specific tax measures and to implement tax laws through regulations issued by presidential decree.

Panama's income tax law went into effect in 1941 and has been amended several times. The latest complete revision was enacted in December 1964 and was implemented by presidential decree in June 1965. Numerous amending decrees have been issued since then.

Municipal taxes (14.12) are assessed directly by the municipalities, which establish the valuations and bases necessary for tax purposes.

1.02 Tax Administration

The Ministry of Finance and Treasury, which corresponds to the Treasury Department in the United States, has overall responsibility for the administration of taxes. The ordinary everyday matters that concern taxpayers are handled by a subordinate body called the General Directorate of Revenue. The General Directorate of Revenue, analogous to the Internal Revenue Service in the United States, is the division of the Ministry of Finance and Treasury that has immediate responsibility for carrying out and administering the tax policies. This body is headed by a Director General.

1.03 Judicial Review

A taxpayer who disagrees with a decision of the tax authorities may file an appeal within 15 working days after the date of the assessment notice. The appeal is in the form of a letter to the office of the General Directorate of Revenue. If the taxpayer does not file an appeal within 15 working days, he may pay the assessment without prejudice and still have six months within which to file an appeal.

In such case, if the decision is favorable to the taxpayer, the excess taxes paid must be returned to the taxpayer within one month after the date of the decision.

A taxpayer who disagrees with the decision of the General Directorate of Revenue may appeal to the office of the Administrator General of Internal Revenue. Such an appeal does not prejudice a later appeal to the executive body or to the Supreme Court.

1.04 Taxes Imposed by Local Authorities

The principal taxes imposed by municipalities are on the issuance of license plates and the sale of alcoholic beverages. Other local and national taxes are discussed in Chapter 13.

Distinctive Features of the Panamanian Tax System

2.01 Summary

Income in Panama is taxed at rates that increase as taxable income increases. Individual income tax is based on its own rate table, but legal entities are subject to one of three rate tables: one for corporations operating in the Republic of Panama, and two tables (depending on date business commenced) for companies operating in the Colon Free Zone (Chapter 3). Branches and partnerships, with the exception of partnerships of lawyers, are taxed as corporations.

Only income from a source within Panama is subject to tax, regardless of residence, nationality, domicile, or the place where contracts are concluded (2.03).

Panama does not treat capital gains differently from ordinary income, with some exceptions (6.05).

Most dividends, and certain other profit distributions, are subject to a 10% withholding tax. This is a final tax and the dividends are not includible in the taxpayer's gross income (6.04).

2.02 Classification of Taxpayers

Panamanian tax laws classify taxpayers into two broad categories:

- Individual taxpayers with or without business activities
- Corporations, branches or agencies, partnerships, undivided inheritance estates, trusts, and other permanent establishments of nonresident individuals

The legal forms of doing business in Panama and their tax effects are discussed in the following paragraphs.

Sole Proprietorships. A sole proprietorship is a legal entity that allows the business activities of an individual to be conducted apart from his other personal activities. However, a sole proprietorship and the individual owner are treated as one taxpayer for tax purposes.

Corporations. The stock corporation is the entity used by most resident and foreign investors. It provides the usual limitation of investors' liability and may be formed by two adults of any nationality. There are no minimum or maximum capital requirements. Corporations may issue bearer shares only if they are fully paid and nonassessable.

Corporations are subject to income tax in accordance with the general rules on Panamanian-source income. Corporations operating in the Colon Free Zone are taxed at special lower rates (2.04). A tax is generally required to be withheld on dividends distributed from Panamanian-source income, but not on certain dividends from the

Colon Free Zone (5.02 and 6.04). This withholding is considered a final tax and no further reporting to Panama is required by the recipient of the dividends.

Companies that are organized under the laws of Panama but do not intend to engage in business in the Republic and have no Panamanian-source income are granted certain benefits. Such companies are not subject to income tax in Panama and are not required to file income tax returns.

A corporation's accounting period may be either a calendar or fiscal year. Authorization of the General Directorate of Revenue is required to adopt a fiscal year. Authorization is also required for any change after an accounting period has been selected.

Agencies and Branches. A commercial license must be obtained to operate in the Republic of Panama as a branch or agency of a foreign company. These entities are taxed as corporations. At the end of their fiscal year, their after-tax profits are treated as having been distributed as dividends and are subject to the withholding tax on dividends (5.02).

Limited Liability Companies. The formation of a limited liability company requires a minimum of two partners who are not married to each other and a maximum of 20 partners. Partners' capital cannot be less than B/.2,000* nor in excess of B/.500,000, and is in the form of nonnegotiable participations. Such participations must be in multiples of B/.100. The participations must be fully subscribed and at least 50% must be paid in cash within five years. Payments in kind must be paid at the time of formation.

The liability of the partners in a limited liability company is limited to the capital invested. The income of a limited liability company is taxed in the same manner as that of a domestic corporation. This form of association is not widely used by foreign investors.

Partnerships. Partnerships may be organized in two forms. One form is the *sociedad colectiva* in which all partners are jointly and separately liable for all actions taken by any partner in the firm's name, although certain partners may limit their liability if such is clearly indicated in the partnership agreement and the term "limited" is included in the operating name. The other form is *sociedad en comandita*, which is composed of both general partners and limited partners. Among other legal differences between these forms of

*B/. stands for Panamanian balboa.

partnerships, limited partners are liable only to the extent of capital invested, provided the names of limited partners are not part of the firm's name and they do not participate in management.

As a general rule, partnerships pay income tax at the same rates as corporations. No deductions are allowed for salaries or any other payments to partners. Distributions of net earnings to partners are subject to the 10% dividend or participation tax (5.02 and 6.04). The complementary tax on undistributed earnings applies in the same manner as to corporations (9.02). An exception to these general rules applies to law firms. Such firms may deduct distributions to their partners and the 10% dividend and complementary taxes do not apply. Partners of law firms include distributions received in their individual income tax returns and pay income tax at the same rates as other individuals.

2.03 Territorial Concept of Income Taxation

Panama assesses taxes only on income from activities within the Republic of Panama, regardless of where such income is received. These activities include exploitation of the land or its minerals; manufacture, construction, transfer, exchange, or grant of the use or enjoyment of real or personal property (both tangible and intangible); and the performance of services by transients as well as residents. This Panamanian-source income is subject to income tax, unless specifically exempt, without regard to the nationality, domicile, or residence of the taxpayer or the place where a contract is executed. Foreign-source income is not subject to tax in Panama. Tax incentives are offered to encourage capital investment (2.04 and 2.05). See 2.04 for taxation within the Colon Free Zone.

The territorial concept also applies to deductions. To be deductible, an expense must be related to the production of income or to the maintenance of its source (7.01). The place of payment is not material for this purpose. Expenditures paid or incurred in obtaining both foreign and domestic income must be allocated on the basis of the taxpayer's books and records or on the ratio of taxable income to total income.

Under the territorial concept, income from sales invoices billed from an office in Panama is exempt from income tax if the goods involved do not touch any territory under the jurisdiction of the Republic of Panama. This is considered an "offshore" operation.

2.04 Special Tax Assessments in the Colon Free Zone

Panama has created a 100-acre shipping and processing center on the Atlantic Ocean, which is known as the Colon Free Zone. Many companies utilize it for the tax and other benefits provided. Companies that operate in the Colon Free Zone receive the following special tax advantages:

(a) Income derived from export sales is subject to income tax at the rates enacted by Law No. 24 of April 29, 1975 (Rate Tables).

(b) Companies that had contracts in force with the government on April 29, 1975, remained subject to tax at the prior 1954 income tax rates, which include a surtax of 20% and an overall decrease of 90% (Rate Tables).

(c) Natural persons and legal entities that begin operations in the Colon Free Zone on or after January 1, 1976, pay income taxes for the first five years of operations at the regular tax rates applied to companies operating in Panama, but they receive a 95% discount provided:

- 80% of their income is from exports.
- At least 30 nationals are permanent employees during the fiscal period and this is certified by the social security department.
- Certain investment requirements are satisfied.

Certain other tax credits related to the tax imposed on exports are available to natural persons and legal entities operating in the Colon Free Zone who do not have contracts in force with the Executive Body based on Law No. 27 of December 21, 1950, and Law No. 24 of September 19, 1957. These tax credits are based on the number of nationals permanently employed, as follows:

Number of Employees	**Tax Credit Available (As Percent of Taxable Income)**
30 to 100	.5
101 to 200	1.0
201 and over	1.5

Dividends paid from profits generated by export activities in the Colon Free Zone are exempt from the 10% dividend tax (6.04). However, if such income or dividends are taxable in any foreign country that allows a full or partial credit for the Panamanian taxes at their full rates, the tax for which credit has been given in the foreign country must be paid to Panama.

When the 1954 income tax rates apply, net income of B/.900 or less is not taxed. However, if the net income from export operations exceeds B/.900, the entire amount is taxable. Net earnings of Colon Free Zone companies on sales in the Republic of Panama are subject to the regular corporation income tax rates without any preferential treatment, such as is accorded to income from export sales.

Companies operating in the Colon Free Zone are also exempt from import and export duties on their foreign operations (13.08), from property taxes (13.05), and from certain municipal license taxes (13.12) other than those on motor vehicles (13.11).

Colon Free Zone taxpayers may enter into contracts with the government that will protect them for up to ten years against income tax increases on export operations. Such contracts also guarantee the continuance of all other Colon Free Zone advantages and do not deny the benefit of possible tax decreases.

Employees of Colon Free Zone companies are subject to the full Panamanian income and social security taxes.

2.05 Other Tax Incentives

International Shipping. Income from international maritime commerce earned by ships registered in Panama is tax free, even if the shipping contracts are negotiated and executed in Panama. Owners of ships registered in foreign countries are not subject to tax on income from Panamanian sources if the country of registry provides reciprocal treatment for income earned in that country by ships of the Panamanian merchant marine.

Foreign Motion Picture Producers. Foreign motion picture producers are taxed on an imputed basis. Fifteen percent of the amounts received from local distributors for the right to exhibit their motion pictures is considered taxable income (6.08).

Insurance Companies. Special legislation requires life insurance companies to create a special reserve fund (referred to as a legal reserve). Life insurance companies must allocate, annually, not less than 20% of net profits before income taxes until the fund equals paid-in capital (B/.200,000 minimum), and then 10% of the annual net profits thereafter. Casualty insurance companies must allocate 15% of annual net profits before tax until the fund equals paid-in capital (B/.400,000 minimum), and then 10% of the annual net profits thereafter.

The amounts set aside in these reserve funds are not subject to income taxation. The reserve funds are designed to strengthen the financial position of the insurance companies and must be reinvested in a manner prescribed by law.

Other Tax Incentives. Certain tax incentives are available to industrial enterprises that transform raw materials or intermediate or semimanufactured products into new products, or which produce raw materials arising from sources such as agriculture, fishing, or forestry and transform these raw materials through an integrated industrial process.

The tax incentives include: a deduction from taxable income for investment that increases plant capacity or provides for the production of new products, with certain limitations; exemption from customs duties on imports of equipment, spare parts, raw materials, semiprocessed products, petroleum products, and containers and packing materials used in the manufacturing process; tax certificates based on export sales; and the carryforward of losses incurred during the term of the contract for three years from the date of the loss.

The tax incentives may be granted by the Minister of Commerce and Industry as well as by the Minister of Finance and Treasury. These incentives may be available for a contract period of up to 20 years.

Other tax incentives are available that exempt newly constructed buildings from the payment of real estate taxes for a period of years and that provide income tax deductions for permanent increases in the number of Panamanian employees.

Part 2:
Income Taxes

Deloitte Haskins & Sells

Tax Rates

3.01 Individuals

Individual income is taxed at graduated rates ranging from 2.5% on the first B/.1,000 to 56% on income in excess of B/.200,000, as shown in the Rate Tables.

3.02 Legal Entities

Corporations, branches or agencies, partnerships (excluding law firms), undivided inheritance estates, trusts, and other permanent establishments of nonresident individuals are taxed on business profits derived from Panamanian sources at graduated rates, depending upon taxable income. The rates vary from 20% on taxable income up to B/.30,000 to 50% for amounts in excess of B/.500,000. These rates were established in December 1976 and are shown in detail in the Rate Tables. Corporations must also withhold a tax of 10% on dividends distributed (5.02 and 9.02). See 3.03 for special tax rates applicable to Colon Free Zone companies.

3.03 Colon Free Zone Companies

Companies operating in the Colon Free Zone are subject to tax on income from export operations at rates based on the date operations commenced. Companies operating prior to April 29, 1975, are subject to 1954 income tax rates. These rates range from 2% on the first B/.2,400 to 34% on income over B/.1,000,000, and the tax so determined is subject to a 20% surtax and to a 90% discount. Companies beginning operations after April 29, 1975, are taxed at rates ranging from 2.5% on the first B/.15,000 to 8.5% on income over B/.100,000. See 2.04 for the conditions that must be satisfied to obtain a discount on this tax liability.

As explained at 2.03, the full income tax at the regular current corporate rates is payable on income from domestic operations and, under some circumstances, on the entire income.

Nonresident Enterprises and Individuals. Professonal fees for services rendered by nonresident enterprises or individuals to companies operating in Panama are subject to withholding for income taxes, which is in the nature of a final tax. The rates vary, depending on several factors (5.02).

As a general rule, fees for services are considered income from a Panamanian source if the payor is deducting such amount to arrive at taxable income.

Returns, Assessments, and Payment of Tax

4.01 Returns and Assessments

The General Directorate of Revenue issues the necessary forms for the filing of tax returns. All taxpayers must file returns except persons who have no other income except dividends and are employed by only one employer or receive a social security pension. If a tax return is not required, the tax withheld constitutes a final tax. Employers who withhold tax on wages must prepare an annual report listing all employees and the amount of tax withheld.

Tax returns must be filed by employees with more than one employer or with taxable income from other than employment. Returns are also required if employees wish to claim itemized deductions (10.02). There is no requirement for filing a consolidated tax return (9.03).

Information required to be filed with tax returns includes details of income and expenses; comparative balance sheets; an explanation of the method of valuing inventories; and payments of dividends, interest, and compensation to stockholders, partners, and creditors. The tax returns of taxpayers with capital exceeding B/.100,000 or annual sales exceeding B/.50,000 must be prepared and countersigned by a public accountant certified in Panama.

Tax returns must be filed within three months after the close of the taxable year. Companies in liquidation must file a return within 30 days following the termination date. Taxpayers are allowed to file returns for years ending on other than December 31, but must obtain prior permission from the Directorate. Returns for periods of less than one year by new or liquidated companies are treated as returns for full taxable years. Companies changing their taxable year must annualize their income for the short period to determine the appropriate rate of tax.

Resident taxpayers and nonresidents who have been in Panama for longer than one month are required to obtain a clearance certificate when leaving the country. This is obtained by showing that all tax payments have been made (13.04).

Nonresidents with Panamanian-source income, other than dividends on which the 10% tax has been withheld (5.02), must file a return personally or through an agent. Any tax payable after deducting withholding taxes (5.02) is due in one payment by March 31 of each year. If a nonresident does not file, the Directorate may use any information available to determine the tax due and may require the appropriate tax to be withheld from future payments by a withholding agent.

Returns are filed in triplicate at the various offices of the Directorate. One copy of the return is stamped, dated, and returned to the taxpayer as evidence of filing.

All original returns are forwarded to the Central Office in Panama City for checking against taxpayer lists, for statistical data, as well as for reviewing the deductions and arithmetical accuracy.

4.02 Payment of Tax

Taxes are payable at offices of the General Directorate of Revenue or at branches of the National Bank. Payments may be by cash, bank transfer, or certified check. Personal checks are not accepted.

Income tax is payable in advance by all companies except for export operations in the Colon Free Zone that are not required to pay estimated taxes. Therefore, the taxpayer must file a declaration of the current year's estimated income along with his tax return reporting the actual income of the prior year. Such estimated income may not be lower than the preceding year's actual income. If actual income should be less than the estimated income for any year, the resulting credit can be applied against the estimated tax on the following year's income or, if it exceeds such estimate, it is refunded. An explanation of the factors contributing to the decline in income must be included with the return. Newly formed corporations must also file a declaration of estimated income.

Taxpayers may pay their estimated income tax in three equal instalments. For calendar-year taxpayers, the first instalment is due on June 30, the second on September 30, and the third on December 31. Fiscal-year taxpayers must pay instalments within six months, nine months, and twelve months after the close of their year. Any tax liability remaining after these payments of estimated tax must be paid when the income tax return is filed.

4.03 Examination of Returns

All tax returns are processed by the Panama City tax office. Returns of individuals must show their personal identification number, which every resident of Panama is required to carry. Corporate returns must show the number assigned to them by the Public Registry office.

Tax returns are arithmetically verified and given a cursory review at the time of presentation. At the discretion of the Director General's office, certain returns are selected for examination. The investigator may demand that the taxpayer furnish the books, records, or other information considered necessary to determine the accuracy of the return. If such investigation shows a greater tax liability, the additional assessment must be made within three years after the date of filing. The taxpayer has the right to disagree with such assessment by using the appeal procedures outlined at 1.03.

The statute of limitations for additional assessments or refunds of income taxes in general is seven years from the end of the taxable year. For withholding taxes, it is 15 years from the date the tax should have been withheld.

4.04 Interest and Penalties for Late Filing and Late Payment

Failure to file a timely tax return may result in a fine of from B/.10 to B/.1,000, depending on the amount of tax.

Underpayments of tax are subject to a penalty of 10% of the deficiency, plus an additional 10% if payment is obtained by attachment of the taxpayer's assets. In addition, interest is charged at the rate of 1% per month or fraction thereof.

Withholding Taxes

5.01 Withholding of Income Tax on Wages

Withholding of income tax at the rates and in accordance with the rules explained below is required on payments to all salaried persons. All employers (whether in business, industry, agriculture, mining, professions, or other activities) must withhold income tax from salaries or other remuneration paid to their employees. The amount of tax is based on withholding tables published by the Directorate General of Revenue. The tables give effect to personal exemptions (10.03), which are claimed by the employee in a statement filed with the employer. If the number of exemptions changes, a new statement must be filed. If the employee does not inform the employer of his allowable exemptions, only the basic B/.600 exemption is allowed.

Tax is withheld from each salary payment, whether monthly or on another basis. The tax must be paid to the collector within 15 days after the month in which the withholding was deducted. The payment, accompanied by a withholding tax declaration, is made either at the offices of the Directorate in Panama City or at other offices throughout the country. On or before March 31, employers must furnish a list of their employees, wages and salaries paid, and the amount of tax withheld during the preceding calendar year. A special form is provided for this purpose.

Employees who work for only one employer and have no other income except dividends are not required to file a tax return.

Employees who file a return may claim credit for the taxes withheld.

Employees from whom tax is not withheld because their salary is paid from abroad or for other reasons must remit their own tax to the National Treasury. Such remittance is due monthly or upon receipt of the remuneration, and is based on the same withholding tables.

5.02 Withholding on Interest, Dividends, and Other Payments

In general, income tax must be withheld on payments of dividends from Panamanian-source income to both residents and nonresidents (see below), but not on dividends paid from export profits of Colon Free Zone companies. Interest and other payments to residents are not subject to withholding, but are included in the taxpayer's return as income subject to ordinary tax. Withholding on payments to nonresidents and on dividends is discussed in the following paragraphs.

Withholding on Payments to Nonresidents. Payments of other than dividends to nonresident individuals and foreign corporations are subject to withholding tax at the graduated tax rates of the individual income tax (3.01) or the corporate income tax (3.02). In determining the rate at which income tax is withheld, prior payments during the same year must be taken into account cumulatively. The tax withheld must be remitted to the collector within ten days.

The tax withheld is based on the full payments for interest, commissions, and remuneration for personal services; and on 50% of the payments for rents, royalties (6.06), annuities, and other types of income not specifically mentioned in the law and regulations. Foreign motion picture producers are subject to withholding tax on 15% of the amounts paid to them by local distributors (2.05). Foreign shipping, communications, and insurance companies may select taxation on either of the following bases:

(1) Treat 10% of gross income from Panama as net taxable income and have tax withheld accordingly, or

(2) Determine taxable income in the general manner.

See 4.01 for tax return requirements applicable to nonresidents leaving the country.

Withholding on Dividends. Dividends paid by a corporation in cash or in stock are subject to a 10% withholding tax. However, certain dividends are specifically exempt from this tax. The exempt dividends include dividends received from another corporation that had withheld the 10% tax, dividends paid from non-Panamanian-source income, and dividends paid from export profits of Colon Free Zone companies (6.04).

The 10% withholding tax on dividends is a final tax and the dividends are not includable in the recipient's taxable income. If the tax is not withheld when required, the payer is liable for the tax. Tax withheld must be remitted to the National Treasury on prescribed tax forms within ten days from the date of withholding.

Income Subject to Tax

6.01 The Nature of Income—Nontaxables

The Panama income tax law defines gross income as the aggregate receipts of cash, goods, or securities, without making any deductions. Included are profits from business, industrial, commercial, and agricultural activities; profits from activities in the Colon Free Zone; profits of persons or companies operating utility franchises; salaries, commissions, bonuses, and other remunerations from personal services; rents, interest, and royalties; profits from sales of property; and any other income not specifically exempted. Receipts in kind are taxed at market value at the time of receipt. Gross income less deductions allowed (Chapter 7) is net taxable income. Only income derived from sources within Panama is taxed (2.03).

The tax law specifies many types of income not subject to tax. Generally, these include income exempted by treaty or contract; income of the state or municipalities; income of religious, charitable, and public welfare organizations; subsistence allowances and social security benefits; income of legally registered Panamanian merchant ships from international maritime commerce; interest on government securities; interest on savings and time deposits with banks established in the Republic; royalties received by persons outside of Panama from persons located in the Colon Free Zone; salaries and fees received by certain diplomatic and consular personnel; and prizes from games of chance operated by the government. Inheritances and gifts are subject to a separate tax (Chapter 15) and are not considered income for income tax purposes. Certain fringe benefits do not constitute taxable income, such as reimbursements of living expenses required by government or union contract.

6.02 Investment Income Generally

Investment income with the exception of dividends (5.02 and 6.04) is subject to income tax if it emanates from sources within the Republic of Panama. Rentals of every nature must be included in gross income, and taxable income is the difference between the total rental value and allowable deductions (7.05). If a part of the premises was unoccupied, the taxpayer must show in his return the duration of the vacancy and certain other information. In addition, any improvements by the lessee for which no consideration is given by the lessor must be included in the lessor's gross income at fair market value at the time the lessor regains possession. Similarly, receipts in kind must be included in gross income at their market value at the time received.

6.03 Interest Income

All Panamanian-source interest income is includable in gross income with the exception of interest from government securities, savings accounts, and time deposits in Panamanian banks. The interest on loans made to nonresidents is not Panamanian-source income when the loan and the use of the money are outside of Panama even though the repayment of capital and interest occurs in Panama.

6.04 Dividends

Dividends are not included in taxable income in individual or corporate income tax returns, and expenses incurred in obtaining dividend income are not deductible. Shareholders, however, are taxed at the flat rate of 10% on dividends received, whether in cash or in kind, or in stock of the paying corporation. Such tax is withheld by the paying corporation.

Dividends are not subject to the 10% tax to the extent they are paid from income derived from foreign sources. Dividends paid by Colon Free Zone companies (2.04) are also exempt when paid from export profits. However, if the shareholders receiving such dividends are allowed a foreign tax credit on the dividends at the full rates of the Panamanian income tax, they must pay Panama the entire amount of such credit. If the portion of the income derived from export sources cannot be determined, the entire dividends are subject to the 10% tax.

Corporations that receive dividends on which the 10% tax has been withheld by the paying corporation, or that were paid from exempt sources, need not withhold any tax when they distribute such dividends to their own shareholders. However, such dividends are deemed not to be redistributed until all other income of the current and the preceding years has been distributed as dividends.

See 9.02 for a special tax on undistributed corporate profits.

Distributions of partnership income, subject to certain exceptions (2.02), are treated as dividends for tax purposes and are subject to the 10% dividend tax.

6.05 Capital Gains and Losses

As a general rule, capital gains are not taxable and capital losses are not deductible for both individuals and legal entities. However, capital gains from the transfer of real property are taxable to the extent that proceeds exceed the sum of the following:

(a) the acquisition cost of the property less depreciation, or the value at June 30, 1965, if the property was acquired before that date,

(b) the cost of any improvements to preserve or increase the value of the property, and

(c) the expenses of effecting the transaction.

The gain so computed is divided by the number of full years the property was owned. The result is added to other taxable income for the purpose of determining the effective tax rate that is then applied to the total capital gain. If the property was acquired by gift or inheritance, the acquisition cost is the value used for estate or gift tax purposes (Chapter 15). Losses on sales of real property may be offset against gains from such sales, but any excess losses may not be deducted from any other income nor may they be carried to another year.

Individuals and legal entities are not taxed on profits from the disposition of bonds, stocks, and other corporate securities provided the securities were issued by a company that is registered with the National Securities Commission and at least 25% of the company's assets are located or invested in the national territory. The exemption from tax does not apply if the seller is a dealer in securities or regularly engages in such activities.

Gain on the sale of personal property other than securities is not taxable unless the seller habitually engages in such activities.

6.06 Income from Royalties, Patents, Copyrights, Etc.

Royalties. Only 50% of royalty income is subject to income tax (5.02). Royalties paid to nonresidents must be reduced by the tax withheld. Royalty expenses are fully deductible. Royalties received from companies operating in the Colon Free Zone are not subject to income tax nor are they deductible expenses.

Sales of Intangibles. In determining taxable income from sales of intangible property, a taxpayer is allowed to deduct acquisition, development, registration, and similar costs. If the sales price is payable in instalments, a proportionate amount of the costs may be deducted each year, based on the instalments received during that year.

If there is no way of determining the total amount to be received in instalments, the taxpayer's cost is assumed to equal 10% of the instalments received.

6.07 Insurance Proceeds and Annuities

Compensation for work accidents, insurance in general, and social security benefits are all exempt from income tax.

Holders of life annuities are presumed to have costs equaling 50% of the annual amount received. These holders may deduct such costs from the time the annuities start until the entire investment has been recovered. Any annuity income received after the investment has been recovered is fully taxable.

6.08 Motion Picture Industry

Foreign motion picture producing companies are not allowed a deduction for expenses. However, their net taxable income is deemed to be 15% of the amounts received from local distributors (5.02). For local motion picture distributing companies, the gross profit is deemed to be 50% of the income received from exhibitors. However, it is 75% of such income when a premiere is shown within the territory of the Republic but outside the jurisdiction of the national authorities and if the ticket charge for an adult admission exceeds B/.040.

Deduction Items

7.01 Business Expenses

Panamanian tax law provides for the deduction of costs and expenses that contribute to the production of income and the maintenance of its source. Costs and expenses must generally be documented for their deduction to be allowed. Minor expenses may be deducted without documentation if the General Directorate of Revenue is convinced by the nature of the expense that it was incurred for the production of income, and if undocumented expenses do not exceed 1% of the total expenses for that year that are properly documented. The percentage is 5% for hotels and restaurants.

7.02 Depreciation

Depreciation is mandatory. A deduction for depreciable assets contributing to the production of Panamanian-source income must be taken each year. Depreciation on assets used in the production of foreign as well as exempt income must be allocated proportionately, based on the time the assets are used in the production of each kind of income. Depreciation not claimed in the proper year is lost for tax purposes.

The asset value or basis used for depreciation includes cost, expenditures incurred in preparing the asset for use, and permanent improvements made during the life of the asset. If an improvement prolongs the useful life of an asset, depreciation is computed on the new life and the undepreciated basis plus the cost of the improvement. Salvage value must be deducted from the depreciation base. Ordinary repairs, maintenance, and similar expenses are deductible from income, provided they do not prolong the life of the asset or result in an enlargement or definite improvement of the original asset. Ordinary repairs are those that do not in any fiscal year exceed 3% of an asset's original value, plus the cost of permanent improvements. If imported assets are valued at more than market value in the foreign country plus transportation and installation costs, the excess is not deductible nor depreciable for income tax purposes.

Depreciation is normally calculated on the straight-line method at rates that have been established by the tax authorities and must normally be used by the taxpayer. The maximum depreciation rates that the tax authorities accept for normal depreciation are listed in the table at Appendix A. Assets that are not listed in the table may be depreciated at the same rate as a similar asset that is listed. If a similar asset is not listed, the taxpayer may not use a depreciation rate in excess of 5% a year, unless the higher rate is authorized by the General Directorate of Revenue.

Regulations also permit the use of the declining-balance and sum-of-the-years digits methods. If the declining-balance method is used, the allowable rate is 125% of the rates shown in Appendix A. The tax authorities may grant permission to use higher rates if an advance written request provides sufficient valid reasons for such authorization. Once a depreciation method has been adopted, it cannot be changed.

Extraordinary losses of depreciable assets are deductible as expenses of the year in which the losses occur. The amount deductible is calculated by subtracting from the undepreciated asset balance any insurance received and any estimated value the asset may still have.

An asset that becomes obsolete may be treated in one of two ways:

(a) The taxpayer may continue to depreciate the asset until its cost is extinguished, or

(b) With the prior authorization of the General Directorate of Revenue, the taxpayer may write off the entire undepreciated balance, less salvage value, at the moment the asset becomes obsolete.

Leasehold improvements may be written off by the lessee over not less than ten years. If occupancy ends before ten years, the remaining balance is deductible in the last year of occupancy.

Amortization of Intangibles. Organization expenses may be deducted as an expense of the year in which they are paid or incurred, or may be amortized in five equal annual instalments. Other intangible assets are generally not deductible or amortizable, including goodwill, trademarks, as well as industrial patents and formulas.

7.03 Depletion

A deduction is allowed for the depletion of mines, quarries, and other natural resources. The deduction for depletion continues during the extraction process until the costs and expenses of obtaining the asset are amortized. The annual deduction for depletion is calculated by estimating the total yield of the natural resource and relating this yield to the units extracted each year.

7.04 Bad Debts

Bad debts may be charged off as operating losses when they become uncollectable, or a reserve may be established to provide for such losses, at the option of the taxpayer.

If the taxpayer elects to use the reserve method, the maximum annual provision is limited to 1% of the total credit sales of goods and services. At no time may the reserve exceed 10% of the balance in notes and accounts receivable at the end of the accounting period. Once adopted, the reserve method may be changed by making the necessary adjustments in the year of change and so advising the Director General of Income.

7.05 Payments of Rents, Royalties, and Technical Service Fees

Taxpayers with rental income are entitled to deduct, in the fiscal year in which they occur, national and municipal assessments and taxes charged against the real estate, as well as depreciation, interest, uncollectable accounts, and any other expenses related to the production of rental income. In addition, the taxpayer has the option of deducting another group of expenses or, in lieu of the actual expenses, deducting 15% of the value of annual rental income. Included in this expense group are repairs and maintenance; wages and salaries, administrative expenses; and the costs of services not paid by the tenant such as water, electricity, and insurance. If the owner occupies a portion of the premises, only the portion of expenses pertaining to the rental premises is deductible.

Royalties are generally deductible for purposes of the income tax on legal entities except by those entities established in the Colon Free Zone.

Technical services fees are deductible provided they contribute to the production of income and the maintenance of its source. Amounts remitted abroad may be subject to income tax withholding (2.03 and 5.02).

7.06 Taxes

All taxes actually paid during the year are deductible, except for income tax itself and any taxes related to foreign income. Penalties for the violation of tax or other laws are not deductible.

7.07 Interest

Interest payments by natural persons and legal entities are generally deductible when the borrowed funds are used in the production of income. However, interest payments on loans obtained from foreign sources are deductible only if the lenders pay income tax on the interest they receive on local loans. Interest payments by individuals, such as on home mortgages, are not allowed as an itemized deduction (10.02).

7.08 Operating Losses

The tax law has no provisions allowing operating losses to be carried to other years. As an incentive under certain contracts, companies may carry losses forward for three years (2.05).

7.09 Employee Compensation and Benefits

Employee compensation is fully deductible if the services rendered are for the production of taxable income and there is no disproportion between the services rendered and the wages paid. The payment of a 13th-month bonus is mandatory under the labor law and is fully deductible. With the exception of lawyers in a law partnership, partnerships are not allowed to deduct any kind of remuneration to partners (2.02).

Profit sharing and other forms of extraordinary remuneration are deductible within limits. The annual amount may not exceed the equivalent of one month's salary, up to a maximum of B/.750 annually, for each employee, and the total payments to all employees for such purposes may not exceed 10% of the taxable income of the entity.

Employee benefits (primarily severance indemnities), as set forth in the work code, are deductible when paid or incurred to the extent that they are not covered by insurance. A reserve for such benefits may be set up by annual deductible provisions of 3% of total employee compensation, but the balance in the reserve at the end of any year may not exceed one-twelfth of the total remuneration paid during that year. When this reserve method is used, employee benefit payments must be charged to the reserve. Should the reserve be insufficient to absorb these payments, the deficiency may be charged to operations.

7.10 Casualty Losses

Casualty losses on assets held for the production of income are deductible to the extent not covered by insurance. The taxpayer must establish that the casualty loss was suffered in good faith, that the amount of the loss agrees with the taxpayer's records and gives effect to depreciation to the date of the loss, and that the deduction reflects any indemnification and salvage value.

7.11 Charitable Contributions

Donations to nonprofit associations for charitable, religious, artistic, cultural, scientific, or similar purposes are deductible from business income if the nonprofit associations are registered with the General Directorate of Revenue. Donations to nonregistered recipients are not deductible. Donations by individual taxpayers are not deductible.

7.12 Advertising, Entertainment, and Travel Expenses

Advertising expenses in the usual form (newspaper advertisements, radio and television commercials, and similar promotions) are deductible.

Entertainment of clients and others commercially related to the taxpayer is deductible. However, such expenses must be supported by vouchers that provide sufficient detailed information to permit the determination of the specific purpose and nature of the entertainment; otherwise, the expense is not deductible. Liquor expenses are normally disallowed. Total entertainment costs may not exceed 2% of gross income.

Individuals who receive remuneration of more than B/.6,000 a year must add any fixed expense allowances to gross income and may deduct 25% of the allowances up to a maximum of B/.3,000 per year.

Travel expenses within or outside the country are deductible provided: (1) such expenses are required for the production of income or the conservation of its source, and (2) the amounts are properly documented and reasonably related to the results of the effort that prompted the travel.

7.13 Insurance

Insurance premiums are deductible if the risks covered are related to persons or property employed in the production of income. Premiums for fire, theft, public liability, workmen's compensation, and travel insurance are generally deductible.

7.14 Nondeductibles

Generally, expenses not incurred in the production of income are not deductible. This category includes personal or living expenses that cannot be shown to be income producing to the satisfaction of the General Directorate of Revenue. In addition, several types of disbursements are specifically classified as nondeductible:

- Interest on loans in excess of the legal rate
- Interest on a sole proprietor's invested capital and on preferred shares of a company
- Losses incurred in prior fiscal years
- Permanent improvements that increase the basis of depreciable property (7.02)
- Expenses of motion picture producing companies (6.08)
- Contributions to organizations not registered with the Directorate
- Bonuses to employees in excess of the limits noted in 7.09
- Amounts spent on lottery tickets

When costs or expenses are paid or incurred in obtaining exempt or foreign income as well as Panamanian-source income, the portion of the cost corresponding to nontaxable income is not deductible (2.03).

Accounting for Income and Expenses

8.01 Tax Accounting Generally

Accounting practices in Panama generally follow those of the United States. The General Directorate of Revenue permits taxpayers to use any generally accepted accounting system. Whatever system is used must be applied consistently and both receipts and disbursements must be handled the same way.

Corporations and limited partnerships may operate on either a calendar- or fiscal-year basis. However, approval of the General Directorate of Revenue is required for adoption of the fiscal-year basis. A fiscal-year taxpayer may select the end of any month as the close of its accounting period. All taxpayers other than corporations and limited partnerships must report on a calendar-year basis.

8.02 Accrual of Business Income and Expenses

Taxpayers are permitted to select either the cash or accrual basis of reporting income. After a basis has been selected, it can be changed by notifying the General Directorate of Revenue and making the necessary adjustments in the year of change. The accrual basis of reporting income is the one most used. As an exception, revenues and costs related to the rental of buildings must be declared in the year accrued and not in the year of actual receipt or disbursement.

8.03 Long-Term Contracts and Instalment Sales

Construction companies may report income in any of three ways: (1) report actual receipts and disbursements on a cash basis, (2) report a portion of the estimated profit according to the percentage of completion, and (3) attribute the entire income and expense to the year of completion.

The use of the instalment sales method of reporting income is not provided for in Panama's income tax laws.

8.04 Inventories

A physical inventory must be taken at least once a year. Generally, inventories must be valued at acquisition cost plus other expenses, such as freight, insurance, and import duties. The methods used to determine acquisition cost may be FIFO (applied on the basis of the cost of the last purchase), LIFO (applied on the basis of the cost of the first purchase), and average cost. Manufacturers must include production costs in valuing goods in process. Semi-finished or finished goods on hand must be valued reasonably according to the stage of completion. When oil or other natural resources extracted by the taxpayer form part of the inventory, the costs of exploration and drilling are not included in the value of such inventory.

Agricultural products are valued by aggregating all costs incurred in raising and preparing them for sale. Purchased domestic animals should be valued either at acquisition cost or the wholesale cash price in the region. Farm animals raised by the agriculturalist are valued at the wholesale cash market price in the region.

Other inventory methods are allowable, but only with the consent of the General Directorate of Revenue. Once a method has been used, it cannot be changed without similar consent. After an authorized change, another change cannot be made for five years.

8.05 Required Books and Records

The Commercial Code requires taxpayers deriving income from commercial or industrial activities in the Republic of Panama to maintain the following books: a general ledger, a book of original entry (general journal), and a book containing yearly entries of inventories and balances (assets and liabilities). These legally required books must be bound, sealed (stamped on each page), and signed by a judge before they are used. In addition, corporations are required to maintain a stock register and a minute book with the same formalities.

Professionals or others working independently must keep a detailed register of fees and other income received during the year as well as the costs and expenses necessary to obtain the income. Such information as the names of clients as well as the nature and dates of services performed, unless of a confidential nature, must be included in the register.

The Commercial Code requires all legal books of account to be preserved while the business is in existence and for five years after it has ceased to exist.

The taxpayer can maintain any auxiliary records deemed necessary for the proper conduct of his business. These books do not have to be legalized as they are not required by the Commercial Code. Therefore, such books may be maintained in any form the taxpayer finds desirable.

Provisions Peculiar to Corporations

9.01 Resident and Nonresident Corporations Compared

A corporation is resident in Panama, regardless of where it was organized, if its principal business is in the Republic of Panama. However, the distinction between resident and nonresident corporations is of less relevance than in some other countries. This is because of the concept of territoriality (2.03), under which only income derived from Panamanian sources is taxable.

The branch of a foreign corporation is subject to income tax on the same basis as a corporation; that is, to the extent the income of the branch has its source in Panama.

9.02 Tax on Accumulated Profits (Complementary Tax)

Panama does not impose a tax on accumulated profits, but it does impose a complementary tax on insufficient distributions of dividends or profits. The complementary tax is a prepaid dividend tax.

Corporate dividends in cash or stock paid from Panamanian-source income are subject to a 10% withholding tax. This is a final tax. The dividends are not included in the recipient's taxable income and the recipient cannot use the 10% tax withheld as a prepayment of income tax.

For any year in which a corporation does not pay dividends, the complementary tax is imposed. This tax is 10% of 40% of the net earnings for that year (an effective tax rate of 4%). The complementary tax is imposed even if the corporation cannot legally pay dividends because it has an accumulated deficit. If dividends are paid that amount to less than 40% of that year's earnings, the complementary tax is 10% of the amount by which the dividends paid fall short of 40% of "net earnings." For this purpose, "net earnings" means net income from Panamanian sources, whether or not subject to tax, less Panamanian income tax. Dividends are considered paid if they are distributed prior to the date the income tax return for the year is due (4.01). The complementary tax is payable at the same time as the corporate income tax. When undistributed profits subject to the complementary tax are distributed in a later year, the company may apply the tax paid (4%) against the dividend withholding tax (10%) and remit the difference (6%) to the National Treasury.

In the case of branches, all taxable income, less income tax, is considered as having been distributed at the end of each taxable year and is subject to the regular withholdinging tax of 10%. This tax is payable when the income tax return is filed.

9.03 Affiliated Corporations

There are no provisions for combining the income and loss of affiliated corporations for tax purposes. The fragmentation of a business into several corporations, therefore, may provide tax benefits because of the graduated scale of tax rates.

9.04 Legal Reserve

Corporations in Panama are not required to establish a legal reserve.

9.05 Liquidations and Other Corporate Changes

Within 30 days after the termination of a business, every natural and legal person must file a final tax return and pay any taxes owed. Any unused balances in reserve accounts, such as the reserves for bad debts and for social benefits, are considered income in the year of dissolution.

Assets distributed to partners or shareholders are valued at their fair market value at the date of distribution and any resulting gain or loss is taxed to the legal entity under the general rules. Retained earnings from a Panamanian source that is distributed in cash or in kind during the liquidation is subject to the 10% dividend tax.

Corporations may acquire their own shares and retire them or hold them as treasury shares, but only if such acquisition does not result in the company having an equity-deficit position.

Corporations may acquire other existing legal entities. An acquisition may involve the assumption of the liability for social benefits, such as employee termination indemnities and seniority premium payments. As these liabilities can be material and are not readily apparent, it is important to obtain professional advice in this area.

Provisions Peculiar to Individuals

10.01 General

Individuals are generally subject to the same tax rules as corporations, except that a different rate schedule applies to individuals (3.01). Married couples can file joint or separate returns, but the basic exemption (10.03) is lower on a joint return than on separate returns. The filing election is made each year when the statement of personal exemption is filed with the employer (5.01) or, if salaries are not involved, when the final return is filed with the General Directorate of Revenue.

10.02 Itemized Deductions

Individuals are not allowed any itemized deductions, except for education tax (14.02) and medical expenses, if such medical expenses exceed 5% of taxable income before such deduction. If they exceed 5%, then 100% of such medical expenses are deductible.

10.03 Personal Exemptions

From aggregate gross income, less allowable medical expenses and education tax, a taxpayer may deduct the following personal exemptions each year:

Basic exemption:

For individual taxpayer	B/. 600
For married couple filing jointly	1,000
Exemption for each dependent	150

If the individual's taxable year contains less than 12 months, the exemptions are reduced proportionately.

If a married couple files separate returns, the medical expense deduction and the exemptions for dependents are allowed to only one spouse. The same is true when a dependent is supported by more than one taxpayer. If the parties concerned cannot agree as to who will get the exemption, it is given to the taxpayer with the larger income or, if the incomes are equal, to the husband or to the older taxpayer.

Minor persons, adults who are mentally or physically disabled, and students supported by the taxpayer are considered dependents. Minors are considered dependents if they live with the taxpayer and their income is not more than B/.150 a year. If the taxpayer is not legally liable for the support of a dependent, a certificate must be obtained from the municipal authorities containing information about the nature of the dependency. No certificate is necessary if support is required by the Civil Code or for ascendants of the taxpayer who are at least 60 years old. For an adult student, a certificate from the school must be supplied. However, the exemption will be denied if the studies began five or more years ago and the student has not passed examinations in at least two courses of study in the last two years.

10.04 Resident and Nonresident Individuals Compared

Persons who live in the Republic of Panama more than 180 days in any fiscal year are considered residents for that year. However, the nationality or residence of a person does not affect the liability for income taxes. Anyone who receives income from a source within Panama is subject to the tax (2.03).

Relief from Double Taxation of Foreign Income

11.01 Tax Treaties

Panama has not entered into any treaties with other countries for the avoidance of double taxation.

11.02 Credit for Foreign Income Taxes

Income derived from foreign sources is not subject to Panamanian income tax. Consequently, no credit or deduction is allowed for taxes paid abroad on foreign-source income.

Pensions, Pension Funds, and Other Retirement Benefits

12.01 General

Panama has an obligatory social security system (Chapter 14). A business enterprise that wishes to supplement social security benefits by instituting a pension or annuity plan must present its plan to the Social Security Board for review and approval before the plan can be put into operation. Because of the difficulties connected with this matter, very few companies in Panama have their own pension or annuity plans. If a plan is approved and a separate trust is set up to administer the plan, employer contributions are deductible. Pensions are fully taxable.

Part 3: Other Taxes

Deloitte Haskins & Sells

Taxes on Sales, Property, and Other Transactions

13.01 Public Registry (Recording) Fees

Certain documents (including deeds, articles of incorporation, partnership agreements, and powers of attorney) must be recorded in either the civil or commercial registry. Such registration is both legally required and is necessary to assert such documents against third persons in a court.

Registration fees vary with the nature and amount of the transaction. The fee for the registration of articles of incorporation is based on the authorized capital, as shown in the Rate Tables. When the authorized capital is composed of no-par-value stock, a value of B/.20.00 is assigned to each share for registration purposes.

13.02 Stamp Tax

Fiscal stamps are required on all documents of a public nature, such as passports, exit permits, and diplomas. They are also required on receipts, invoices for credit sales, drafts, notes, and checks. Fiscal stamps are obtainable in denominations ranging from B/.0.01 to B/.20.00.

Stamped paper sold by the government at B/.3.00 a sheet is required for recording documents in the public registry, presenting pleas before courts, and certain other documents.

13.03 Tax on Air Transportation

Foreign travel is taxed at B/.4.00 per B/.100 value or fraction thereof of a ticket purchased in Panama. An airport tax of B/.8.00 is levied on all departing passengers, except those in transit for less than 12 hours.

Tickets for domestic air transportation are subject to a tax of 5% of the fare.

13.04 Clearance Certificates

A clearance certificate indicates that the taxpayer has fulfilled all of his income tax obligations. Such a certificate costs B/.0.25 and is required for the following:

(a) Withdrawing merchandise from customs

(b) Signing contracts with the government or any of its autonomous or semiautonomous institutions

(c) Recording deeds in the public registry

(d) Issuance or renewal of business licenses

(e) Obtaining checks from the national government or municipal offices in payment for services rendered or merchandise sold

(f) Purchasing tickets for trips to foreign countries

These clearance certificates are issued for a specific period. To obtain one, a taxpayer must demonstrate that he is current in his payment of income tax. When one expires, another certificate must be obtained.

The municipality of Panama issues its own clearance certificates. These also cost B/.0.25 and are required for the sole purpose of obtaining new automobile license plates every year.

13.05 Property Tax

Property or real estate is taxed at a progressive scale, as shown in the Rate Tables. Buildings and/or improvements are exempt from the tax for five years after construction is completed.

Complete exemption is granted to properties owned by the state and municipalities as well as by religious, public health and welfare, and educational institutions.

The tax is based on assessed value which is determined by the Land Commission. Assessed values may be set by a general valuation covering the entire territory of the Republic, by a partial valuation for special assessments in certain areas, and by a specific valuation of a single piece of property to take into account improvements, demolitions, or other changes in the character of the property.

13.06 Liquor Tax

A tax of B/.0.35 per degree of alcohol per liter is levied on the manufacture of liquors. Taxes on the production of beer and wine are B/.0.1325 and B/.0.05 per liter, respectively. Exported beer is exempt from the tax. Consumption of alcoholic beverages is taxed through license fees imposed upon wholesale and retail distributors of closed containers and upon bars that dispense liquor from open containers. License fees vary among the cities.

13.07 Taxes on Vessels

Ship registration fees of B/.1.00 per net ton and property taxes of B/.0.20 per registered ton are imposed upon vessels when first put into use. In addition, an annual tax of B/.0.10 per registered ton is levied on ships registered for international commerce with the national merchant marine and of B/.0.05 on other vessels. State and municipally owned vessels and those valued at less than B/.1,000 are exempt from the tax.

13.08 Import and Export Duties

Panama levies import duties on all goods except those legally or contractually exempted. No duties are levied on exports except for bananas, sugar, certain natural resources, scrap metals, and valuable metals.

13.09 Special Taxes on Mineral Extraction and Related Activities

Under the provisions of Panama's Mining Code, mineral concessions may be granted to national or foreign natural persons and legal entities that maintain an authorized attorney-in-fact in Panama, provided the petitioner's technical and financial qualifications have been verified.

Concessions may be granted to carry out the exploration, extraction, transportation, and processing of minerals within the territorial and maritime boundaries of the Republic of Panama as well as within the outer limits of its continental shelf. The rentals, royalties, and taxes covering exploration and production activities are complex and are not covered here. Professional assistance is advisable in these areas.

13.10 Commercial and Industrial Licenses

It is necessary to obtain a license to carry on commercial or industrial activities in Panama. There are two types of licenses:

(1) Commercial (excluding retail) and industrial.

(2) Retail commercial (mainly, mercantile business and representatives and agents of producers). This type of license can only be obtained by Panamanians.

These licenses are taxed annually at the rate of ½% of the net worth of the company, increased by any amounts paid or owed to a parent company or home office.

The license tax must be paid within three months after the close of the fiscal year. Late payments are subject to a 10% surcharge. The minimum tax is B/.5 and the maximum tax is B/.10,000.

13.11 Road Tax

Motor vehicles are subject to a national road tax and to a municipal license tax that varies with the use, size, and type of vehicle.

13.12 Municipal Taxes

Municipalities are authorized to tax many items (1.01). The tax rates vary from one city to another. Municipal business license taxes are usually based on gross sales, production, or paid-in capital. Some municipalities offer a discount if annual taxes are paid before a certain date. Signs, posters, and advertising bills of commercial or industrial establishments are also taxed at rates that vary with the nature and location of the taxable item.

13.13 Value Added Sales Tax

Since March 1, 1977, a 5% tax is imposed on the transfer of personal property by sale and purchase, exchange, contribution to a corporation, cession, or any other act, contract, or agreement that either implies or is aimed at transferring control of the personal property.

The tax on imports is payable when the customs declaration is settled and, in other cases, at the time of transfer. The assessable base is the value of the imports plus the cost of services that benefit the importer, such as transportation, packaging, and interest charges.

The assessable base includes the c.i.f. (cost, insurance, and freight) value plus taxes required to import the item. If the c.i.f. value is not known, it is determined by adding 15% to the f.o.b. value. The tax is not imposed on the following:

(a) Transfers because of death, gift, or acts between living beings which were subject to the inheritance and gift tax

(b) Transfers because of marriage agreements or division of matrimonial goods

(c) Imports, expropriations, and sales by the state

(d) The adjudication of goods arising out of ordinary or special legal proceedings

(e) The transference of negotiable documents and titles of value in general

The following transfers of goods are exempt from the 5% sales tax:

(a) Sales of agricultural, avicultural, livestock, and similar products in their natural state and those subject to a fattening, killing, or refrigeration process only

(b) Sales by fishermen and hunters of products in their natural state or subject to a refrigeration and freezing process only

(c) Exported goods and the reexport of goods imported into the Free Zone

(d) Transfers by authorized agencies of the United States government in the Panama Canal Zone

(e) Transfers in the free zones of the Republic of Panama

(f) Transfers of ownership of personal property in customs areas and official warehouses by endorsement of the proper documents

(g) Transfers of carbonated beverages

(h) Imports and transfers of certain fuel, lubricants, and similar products

(i) Imports and transfers of food items

(j) Imports and transfers of medical and pharmaceutical products specified in Group 541 of the Schedule of Importation

The tax is generally payable within 15 days after the close of each month when the tax return is due. A penalty of 10% and interest of 1% monthly is imposed for late filing. After 60 days, fines of B/.100 to B/.5,000 may be imposed and the establishment may be closed in extreme cases.

The taxpayer may deduct, on his return, the amount of tax he paid during the same period. Such credit is calculated proportionately to the operations that are taxed and exempt from tax during the period. The proportionate share not allowed as a sales tax credit may be considered a deductible expense for income tax purposes.

The Income General Management Office will issue certificates to exempt taxpayers who, because of their activities in export, reexport, and transfer to agencies of the United States in the Panama Canal Zone, will continuously have a credit balance on their sales tax returns.

Because the sales tax is not an import tax, it is not included in the relief from import duties that may be granted under the incentive laws (2.05).

Employment Taxes

14.01 Social Security

Panama has an obligatory social security system that is financed by employer and employee contributions. Employer contributions are deductible. Employee contributions are not deductible and social security benefits are not taxable.

Social security provides benefits for sickness, maternity, old age, and death. Participation is required of all persons employed by private organizations and government entities. Voluntary participation is available to self-employed persons and others. Persons exempt from social security participation include children under 16, parents and spouse of an employer, casual and home workers, persons employed for two months or less, and men and women first entering insurable employment at the ages of 60 and 55, respectively.

Contributions Payable. Employers contribute 8% of monthly payroll to the social security fund. Compulsorily insured persons, pensioners, and the self-employed contribute 6½% of wages, pensions, or profits. Voluntarily insured, other than self-employed persons, contribute 8% of wages or of an amount established by regulations. An additional 5% of the wage or income of the head of a family may be paid for family insurance, which is voluntary.

Contributions are payable within ten days after the end of each month. Surcharges and penalties are assessed for late payment.

14.02 Education Tax

Employers are required to pay an education tax at the rate of 2% of payroll. Of this amount, ¾% is withheld from employees' wages, so the net cost to the employer is 1¼% of payroll. Employers may deduct this tax and employees may treat it as an itemized deduction (10.02).

14.03 Termination Indemnities

The work code requires the payment of termination indemnities, referred to as seniority premiums, to employees who have at least ten years of continuous service and have attained age 40 for men or age 35 for women. This law was enacted December 30, 1971, and provides that employment of up to ten years prior to that date is recognized for purposes of eligibility for termination benefits.

The termination benefit is one week's salary for each year of qualified employment. Salary, for this purpose, is the average of all remuneration, as defined in the code, received during the last five years.

These indemnities are deductible for income tax purposes when payments are made to employees. As an alternative, the employer may enroll in a voluntary plan administered by the Department of Social Security. Under this alternative, the accruing benefits are currently funded and the contributions are currently deductible.

Estate and Gift Taxes

15.01 Estate Taxes

Panama does not directly tax the gross or taxable estate of a decedent. Instead, an inheritance tax is imposed on the amount of each bequest or devise. Although the inheritance tax is based on the amount received by each heir, it is payable from estate funds.

If an inheritance does not exceed B/.3,000, the first B/.1,000 is not subject to tax. The tax rates are graduated in terms of higher rates for both larger inheritances and for inheritors whose relationship to the decedent is more remote. The specific rates are listed in the Rate Tables; a 20% reduction is provided from the tax as computed by those rates.

Taxable inheritances consist of all real and personal property located in the Republic of Panama and owned by the decedent on the date of death. The country where the will is opened or litigated, and bequests made in a foreign country, does not affect the imposition of inheritance tax on property located in Panama.

15.02 Gift Taxes

Gift taxes have the same structure as inheritance taxes, and the same tax rates apply.

Part 4: Rate Tables and Appendices

Income Taxes—Individuals

Income Bracket (B/.)	Tax on Lower Amount (B/.)	Percentage on Excess over Lower Amount
0- 1,000	0	2½
1,000- 2,000	25	3½
2,000- 3,000	60	5
3,000- 4,000	110	6
4,000- 5,000	170	7½
5,000- 6,000	245	9
6,000- 8,000	335	11
8,000- 10,000	555	13
10,000- 15,000	815	17
15,000- 20,000	1,665	19½
20,000- 30,000	2,640	22
30,000- 40,000	4,840	26
40,000- 50,000	7,440	30
50,000- 60,000	10,440	34
60,000- 70,000	13,840	37
70,000- 80,000	17,540	41
80,000- 90,000	21,640	44
90,000-100,000	26,040	48
100,000-200,000	30,840	52
200,000-upwards	82,840	56

Income Taxes—Legal Entities

(Regular income tax rates applied to corporations, branches or agencies, partnerships except law firms, undivided inheritance estates, and other permanent establishments of nonresident individuals)

Income Bracket (B/.)	Tax on Lower Amount (B/.)	Percentage on Excess over Lower Amount
0- 30,000	0	20
30,000-100,000	6,000	30
100,000-500,000	27,000	45
500,000-upwards	207,000	50

Note:

See the following Rate Table for companies operating in the Colon Free Zone.

Income Taxes—Applicable to Net Earnings from Export Trade of Companies Operating in the Colon Free Zone (2.04)

1. Based on 1954 Income Tax Rates

Income Bracket (B/.)	Tax on Lower Amount (B/.)	Percentage on Excess over Lower Amount
0- 2,400	0	2
2,400- 3,600	48	2½
3,600- 4,800	78	3
4,800- 6,000	114	4
6,000- 8,400	162	5
8,400- 12,000	282	6
12,000- 16,800	498	7
16,800- 22,800	834	8
22,800- 30,000	1,314	9
30,000- 40,000	1,962	10¼
40,000- 50,000	2,987	11½
50,000- 60,000	4,137	12¼
60,000- 70,000	5,412	14
70,000- 80,000	6,812	15¼
80,000- 90,000	8,337	16½
90,000- 100,000	9,987	17¾
100,000- 150,000	11,762	19¼
150,000- 200,000	21,387	20¾
200,000- 300,000	31,762	22½
300,000- 400,000	54,262	24¼
400,000- 550,000	78,512	26¼
550,000- 750,000	117,887	28½
750,000-1,000,000	174,887	31
1,000,000-upwards	252,387	34

Important Note: The tax as computed above is increased by a 20% surtax and decreased by a 90% discount.

2. Based on Law No. 24 of April 29, 1975

0- 15,000	0	2.5
15,000- 30,000	375	4.0
30,000-100,000	975	6.0
100,000-upwards	5,175	8.5

Public Registry Fees for Articles of Incorporation (13.01)

Authorized Capital (B/.)	Fee on Lower Amount (B/.)	Rate on Each B/. 1,000 over Lower Amount (B/.)
0- 10,000	20.00	None
10,000- 100,000	20.00	0.75
100,000-1,000,000	87.50	0.50
1,000,000-upwards	537.50	0.10

Property Tax (13.05)

Property Value (B/.)	Tax on Lower Amount (B/.)	Percentage on Excess over Lower Amount
0-10,000	None	None
10,000-20,000	None	1.40
20,000-50,000	140.00	1.75
50,000-75,000	665.00	1.95
75,000-upwards	1,152.50	2.10

Inheritance and Gift Taxes (Chapter 15)

Value of Gift or Bequest (B/.)	A %	B %	C %	D %	E %	F %
1,000- 5,000	4	4¼	4½	4¾	5	5½
5,000- 10,000	5	5¼	5½	5¾	6	6½
10,000- 15,000	6¼	6½	6¾	7	7¼	7¾
15,000- 20,000	7½	7¾	8	8¼	8½	9
20,000- 30,000	9½	9¾	10	10¼	10½	10¾
30,000- 50,000	11¾	12	12¼	12½	12¾	13¼
50,000- 75,000	14	14¼	14½	14¾	15	15½
75,000-100,000	16¼	16½	16¾	17	17¼	17¾
100,000-150,000	19	19¼	19½	19¾	20	20½
150,000-200,000	21¾	22	22¼	22½	22¾	23¼
200,000-300,000	25¼	25½	25¾	26	26¼	26¾
300,000-400,000	28¾	29	29¼	29½	29¾	30¼
400,000-upwards	32¼	32½	32¾	33	33¼	33¾

Key to Table:

A—Lineal descendants, adopted children, and spouse

B—Lineal ancestors

C—Brothers, half-brothers, sisters, half-sisters, sons-in-law, and daughters-in-law

D—Relatives up to the third degree of collateral consanguinity

E—Relatives of fourth degree of collateral consanguinity and up to the second degree of affinity

F—Relatives not included in any of the above groups and non-relatives

Notes:

1. If the bequest does not exceed B/. 3,000, the first B/. 1,000 is not subject to inheritance tax.

2. For the purpose of the tax payment, there is a 20% discount from the tax computed by using the above table.

Depreciation Rates

	(%)
Buildings:	
Metal, concrete, reinforced concrete with or without iron, brick with reinforced concrete columns or with iron or iron alloys	2½
Wood	5
Adobe and other materials not specified	10
Improvements for industrial, commercial, or agricultural use, such as paved roads, sidewalks, canals, drainage ditches, sewers, piers, bridges, and fences	5
Permanent equipment in buildings (elevators, plumbing fixtures, air conditioners, etc.)	5
Rail lines and accessory equipment	4
Office equipment	10
Office furniture:	
Wood	10
Metal	7
Telecommunication installations	15
Transportation equipment:	
Automobiles used in a business or profession	15
Public service automobiles	20
Buses	15
Airplanes	15
Trucks and trailers	15
Railroad locomotives and cars	5
Wooden or plastic (fiberglass) boats	8½
Metal boats	5
Bicycles, tricycles, motorcycles, etc.	25
Fork lifts	10
Other vehicles	10
Industrial machinery and equipment (excluding those specified in other parts of this table):	
Used in the manufacture of construction materials made of stone, cement, clay, or other nonmetallic minerals	5
Used in food processing	7½
Used in refining petroleum and sugar, alcoholic beverages; processing tobacco or vegetable oil; and milling grain	5
Used in industries producing plastics, metallurgy, printing, rubber, wood, furniture, and glass	7½
Used in other industries	8½

(continued)

	(%)
Machinery and equipment used in agriculture and breeding (excluding those specified in other parts of this table):	12½
Construction and earth-moving equipment	15
Tools and small equipment	25
Motors:	
Gasoline and kerosene	10
Diesel, semi-diesel, gas, or steam	7½
Electric	7½
Boilers and steam engines	7½
Electric generators:	
Up to 50 kilowatts	8½
More than 50 kilowatts	4½
Turbines:	
Hydraulic	2½
Steam or gas	4
Electric energy transmission and distribution equipment (towers and poles, insulators, conductors, lightning rods, transformers, substations, control, measuring, and breaking devices):	
Up to 500 volts	4
More than 500 volts	2½
Hotel and restaurant equipment:	
Kitchen utensils	25
Kitchen equipment	10
Porcelain and crystal	50
Carpets	15
Pillows, sheets, blankets, and mattresses	20
Refrigerators	12½
Breeding stock:	
Cattle	15
Swine	25
Fruit-bearing trees and shrubs	3

Specimen Income Tax Computations of a Panamanian Resident Corporation

Computation of Taxable Income:

Gross income		B/. 1,200,000
Less tax-free income: Income from foreign sources	B/. 30,000	
Dividends from Panamanian corporations	10,000	
Interest from Panamanian savings banks	10,000	50,000
Remainder		1,150,000
Operating and administrative expenses	900,000	
Less expenses allocable to foreign income	5,000	895,000
Taxable income		B/. 255,000

Tax Computations:

1. At regular corporate rates (3.02):	
Tax on first B/. 100,000	B/. 27,000
Tax on excess per Rate Table	69,750
Total tax	B/. 96,750
2. At 1954 tax rates applicable to export earnings of Colon Free Zone companies (3.03):	
Tax on first B/. 200,000 (Rate Table)	B/. 31,762
Tax on excess per Rate Table	12,375
	44,137
Plus 20% surtax	8,827
	52,964
Less 90% discount	47,668
Total tax	B/. 5,296
3. At rates effective April 29, 1975, applicable to export earnings of Colon Free Zone companies (3.03):	
Tax on first B/. 100,000	B/. 5,175
Tax on excess per Rate Table	13,175
Total tax	B/. 18,350

Specimen Income Tax Computation of an Individual Taxpayer

Data:

Taxpayer is married with four dependent children. He earns B/. 1,000 per month plus his 13th month bonus of B/. 1,000. His wife has no income. During the year, he pays B/. 669 in medical expenses and an education tax of B/. 98.

Computation of Taxable Income:

Total income for the year		B/. 13,000
Deductions (10.02 and 10.03):		
Annual exemption	B/. 1,000	
Allowance for dependent children (4 × 150)	600	
Education tax	98	
Allowance for medical expenses (taxable income before allowance for medical expense B/. 11,302 × 5% = 565 which exceeds 5% and is, therefore, totally deductible)	669	2,367
Taxable income		B/. 10,633

Computation of Tax:

On first B/. 10,000 per Rate Table	B/. 815
On excess of B/. 633 at 17%	108
Total tax	B/. 923

Taxes on Representative Earned Incomes

Earned Income (B/.)	Single (B/.)	Married (no dependents) (B/.)	Married (2 dependents) (B/.)
2,000	39	25	18
4,000	134	110	95
6,000	281	245	222
8,000	489	445	412
10,000	736	684	645
15,000	1,563	1,495	1,444
20,000	2,523	2,445	2,387
30,000	4,708	4,620	4,554
40,000	7,284	7,180	7,102
50,000	10,320	10,140	10,050
60,000	13,636	13,500	13,398
70,000	17,318	17,170	17,059
80,000	21,394	21,230	21,107
90,000	25,864	25,600	25,468
100,000	30,552	30,360	30,216

Note:

The above tax results are based on the following deductions:

Personal exemptions:

Single person	B/. 600
Married couple	B/. 1,000
Dependents (each)	B/. 150